

**Illinois Department of Transportation
FFY 2006
Overall DBE Goal**

The Illinois Department of Transportation (Department or IDOT) has prepared this submission to the Federal Aviation Administration (FAA) to describe the methodology used to establish the overall Disadvantaged Business Enterprise (DBE) goal mandated by 49 CFR Part 26 for its federally-assisted highway contracts. The Department relied on and followed the regulations and guidance provided concerning the implementation of the regulations. 49 CFR §26.45 requires a two-step process for setting the overall DBE goal that reflects the level of DBE participation on IDOT's contracts expected in the absence of discrimination. The first step is the calculation of a base figure for the relative availability of DBEs. The second step requires consideration of a possible adjustment of the base figure to reflect the effects of the DBE Program and the level of participation that would be expected "but for" the effects of past and current discrimination against DBEs. As further required by § 26.51(c), the Department submits a projection of the portion of the overall goal that it expects to meet through race-neutral means and the basis for the projection.

The Department notes that a decision regarding the constitutionality of its 2005 goal is still pending with the federal district court in *Northern Contracting, Inc. v. IDOT*, No. 00 C 4515, and that FAA has approved IDOT's 2005 goal.

I. Methodology and Evidence

To meet the requirements of § 26.45, the Department commissioned a Disadvantaged Business Enterprise Availability Study (IDOT Study) from National Economic Research Associates, Inc. (NERA), an internationally recognized economics consulting firm (Attachment A). The IDOT Study formed the basis for the Department's 2005 goal, and was relied upon at trial in *Northern Contracting*.

The IDOT Study provides a statistical analysis of baseline DBE availability, and examines econometric evidence of disparities between DBEs and non-DBEs in factors impacting entrepreneurial success on Department contracts and subcontracts. In particular, for Step 1 the IDOT Study estimated statewide DBE availability using data on IDOT's expenditures for highway construction, engineering consulting and aviation construction contracts and subcontracts, and carefully constructed databases of firms in those industries. To address Step 2, the IDOT Study reviewed existing qualitative and quantitative evidence of discrimination and assessed the likelihood that statewide DBE availability would be different if the relevant markets in which IDOT operates were race-neutral; it then estimates the magnitude of this difference. The Study's results are summarized below.

Recent favorable developments in the courts as well as USDOT's approval of IDOT's and other recipients' goals based upon NERA studies give the Department continuing confidence in the Study's methodology, constitutional validity and narrowly tailored results. This approach has been upheld by the Eighth Circuit Court of Appeals in the challenge to the Minnesota Department of Transportation's DBE Program, and by the Tenth Circuit Court of Appeals in holding that the City and County of Denver's local Minority and Women Business Enterprise

Program meets strict constitutional scrutiny.¹ It provides a statistically sound and detailed basis to meet the requirements of Part 26, and more fully addresses the remedial purpose of the DBE Program and Congressional intent than the methodology previously relied upon by the Department. The IDOT Study's data may also assist IDOT in setting contract goals to reach its overall, aspirational DBE goal for federally-assisted contracts. While the underlying availability data were collected some time ago, IDOT's product and geographic marketplaces have remained consistent. Moreover, older estimates of firm availability probably understate current availability, as firms owned by women and minorities continue to make up an ever increasing share of the economy.

A. Step 1 Estimate of Relative Availability of DBEs

1. Definition of IDOT's contracting market

The first element in estimating DBE availability was to determine empirically the relevant product and geographic markets for the Department's federally-assisted contracts. Based upon five years of the Department's contract and subcontract expenditure data, a total of 27 four-digit Standard Industrial Classification (SIC) codes² were identified as IDOT's product market, and the State of Illinois was identified as the geographic market. This approach incorporates the guidance of USDOT to use 4-digit SIC codes and to weight that data by the Department's expenditures. See <http://osdbuweb.dot.gov>. It also separates firms by detailed function, delineating, for example, general contractors from specialty trade firms that primarily act as subcontractors on IDOT projects.

2. Counting establishments in IDOT's relevant markets

The IDOT Study next examined the availability of DBEs in the relevant markets. It used Dun & Bradstreet's *Marketplace* database, an independent and established data source routinely relied upon by courts, to identify the total number of Illinois businesses in each four-digit SIC code, weighted by that code's share of IDOT's product market. It next identified the number of firms owned by minorities and women, based upon the information in *Marketplace*, the Department's DBE directory and other regional listings. As noted by USDOT's guidance, supplementing the DBE Directory with other information on minority- and women-owned firms may provide a more complete picture of the availability of firms to work on the Department contracts than reliance solely upon the number of IDOT certified and prequalified and preregistered DBEs. Because of the possible misclassification and non-classification of firms from these sources, additional scientifically accepted safeguards were taken to verify listed DBEs and estimate unlisted DBEs.

3. Estimating baseline DBE availability

Using empirical market definitions, business establishment data and statistical verification surveys, the Study estimated 22.77% as the base availability figure for Step 1.

B. Step 2 Consideration of Adjustment to the Base Figure

¹ *Sherbrooke Turf, Inc. v. Minnesota Department of Transportation*, 345 F.3d 964 (8th Cir. 2003), *cert. denied*, 124 S.Ct. 2158 (2004); *Concrete Works of Colorado Inc. v. City and County of Denver*, 321 F.3d 950 (10th Cir. 2003), *cert. denied*, 124 S.Ct. 556 (2003). See also *Builders Association of Greater Chicago v. City of Chicago*, 298 F.Supp.2d 725 (N. D. Ill. 2003) (*BAGC*).

² SIC codes can easily be converted into the North American Industry Classification System (NAICS) codes now adopted by the U.S. Census Bureau.

Step 2 requires that the Department examine all evidence in its jurisdiction to determine what adjustment, if any, is needed to the base figure to arrive at the overall goal. Included among the types of evidence that must be considered are the current capacity of DBEs to perform work on the Department's federally-assisted contracts, as measured by the volume of work DBEs have performed in recent years, and evidence from disparity studies conducted anywhere within IDOT's jurisdiction, to the extent not already accounted for in the base figure. The Department may also consider available evidence from related fields that affect the opportunities for DBEs to form, grow and compete. These include, but are not limited to, statistical disparities in the ability of DBEs to get the financing, bonding and insurance required to participate in the Program, and data on employment, self-employment, education, training and union apprenticeship programs, to the extent relevant to the opportunities for DBEs to perform in the Program. The regulations caution that any adjustment to the base figure to account for the continuing effects of past discrimination or the effects of an ongoing DBE program must be based on "demonstrable evidence that is logically and directly related to the effect for which the adjustment is sought." §26.45(d)(3). Each of these categories is discussed separately below.

1. Past DBE Utilization

IDOT considered the current capacity of DBEs to perform on its federally-assisted contracts, measured by the volume of work DBEs have received in recent years. For FFYs 2002- 2004, DBEs received 12.27% of the contract commitments (\$607,432,996 of \$4,969,285,499 of total awards). For the period from April 2004 through March 2005, DBEs received 14.15% of the total awards (\$244,043,230 of \$1,687,654,474 of total awards).

2. Evidence from local disparity studies

As discussed in the IDOT Study, several Chicago area governments have conducted studies since *City of Richmond v. J. A. Croson*³ to examine the extent, if any, that construction industry discrimination has affected DBE's. These studies suggest that the availability of DBEs in Illinois to do business with the public sector has been depressed by the persistent effects of discrimination. However, IDOT is not relying upon these studies because of their age.

The Department also reviewed and relied upon the 2000 Disadvantaged Business Enterprise Availability Study for the Northeast Illinois Regional Commuter Railroad Corporation D/B/A Metra (Metra Study) (Attachment B). This Study encompassed the Chicago region and was prepared to meet METRA's responsibilities under Part 26. The Metra Study's findings suggest that discrimination may be impacting the ability of DBEs to compete for IDOT's contracts. In addition to the Step 1 availability estimate, the Study included mail surveys to quantify and compare anecdotal evidence on the experiences of DBEs and non-DBEs in construction. Overall, more than 20 percent of DBEs in the trades and professional services reported discrimination in (1) working or attempting to work on public sector subcontracts; (2) working or attempting to work on private sector subcontracts; (3) working or attempting to work on public sector prime contracts; (4) working or attempting to work on private prime contracts; (5) receiving payment for work performed; (6) applying for commercial loans; and (7) encountering double standards in quality, inspection or performance requirements. Almost 51% of DBEs in the trades and 54% in professional services reported that they were seldom or never solicited by prime contractors for projects without participation goals. To test whether DBEs find procurement more difficult because they are smaller or newer firms than non-DBEs and not because of direct discrimination, the Study applied Probit regressions, with the independent

³ 488 U.S. 469 (1989).

variables being age of the firm, number of employees and firm revenues. Statistically significant disparities in the business experiences of DBEs and non-DBEs remained after controlling for these firm characteristics. The Metra Study also examined whether DBEs suffer discrimination in the market for business capital. Based upon data from the Federal Reserve Board and the U.S. Small Business Administration, the Study concluded that loan applications from minority-owned firms were substantially more likely to be denied than those from other groups, even after controlling for differences in size and credit history. Further, minority-owned firms granted loans paid higher interest rates than comparable white-owned firms.

Although not labeled a “disparity study,” the City of Chicago recently commissioned expert reports examining statistical disparities in the Chicago area construction industry, in connection with its revisions of its Minority- and Women-Owned Business Enterprise (M/WBE) Construction Program. These studies were in addition to the extensive statistical analyses relied upon by the court in *BAGC* in holding that Chicago had presented strong evidence of discrimination in the construction market sufficient to meet strict constitutional scrutiny. Trial expert reports also documented that the capacity of firms in the construction industry is relatively elastic, demonstrating that minority- and women-owned firms are available to perform additional work. Chicago’s 2004 reports analyzed the 2000 Decennial Census of Population Public Use Microdata Sample (PUMS), the most detailed, individual data available. The experts found that the probability of being self-employed in the Chicago construction market remains lower for minorities and White women than for similar White men, and that self-employed White men working in the region’s construction industry had considerably higher earnings and worked more hours, relative to similar self-employed Blacks, Hispanics, Asians and White women. The experts opined that the most plausible explanatory variable for the statistically significance differences in business formation and business success was minority status and gender. The Department considered and relied upon this evidence as well.

3. Statistical evidence of disparities

a. IDOT Study

To provide a quantitative analysis of the effects of discrimination in IDOT’s marketplace, the IDOT Study examined disparities in Illinois in earnings and business formation rates between DBEs and non-DBEs based upon the 2000 PUMS and Census Bureau’s Current Population Survey (CPS).

i. Disparities in earnings

The Study analyzed whether minority and female entrepreneurs earn less from their businesses than do their White male counterparts. Other things equal, if minority business owners as a group have lower earnings from their businesses than comparable non-minorities, economic theory suggests that minority business failure rates will be higher and minority business formation rates will be lower than those that would be observed in a race-neutral marketplace. Applying linear regression to assess whether minorities earn less than Whites with similar characteristics, the Study concluded that similarly situated minorities and women, especially Blacks, earn less than their comparable White male counterparts.

ii. Disparities in business formation

Likewise, the Study examined whether more minority businesses would have been formed if minorities were as likely to own their own businesses as were similarly situated White males, and if so, how many more such businesses would have been expected to be formed but for

discrimination. Using Probit regression to control for age, industry and education, the Study found large and statistically significant disparities in the business formation rate for DBEs.

iii. DBE availability “but for” discrimination

Using the statistical data on disparities, the Study estimated that DBE availability in Illinois in a race-neutral market would be approximately 20.8% higher than the Step 1 estimate, for an estimated availability of DBEs “but for” discrimination of 27.51% in a fully race-neutral market. The base figure is depressed because discrimination has impacted the likelihood that minorities and women will become entrepreneurs and that when they do; those firms are likely to be less profitable and to fail more frequently.

b. Disparities in access to commercial credit

The Department also examined expert reports submitted in the *BAGC* trial concerning disparities in the access of minority- and women-owned construction firms to commercial credit. This testimony established that minority-owned businesses face impediments to obtaining credit that go beyond observable differences in their creditworthiness. Loan denial rates were significantly higher for minority-owned firms than for white-owned firms, controlling for measures of assets, liabilities, creditworthiness and other characteristics. This result was largely insensitive to changes in econometric specification. Overall, the evidence is consistent that minority-owned firms are disadvantaged in the credit market. This evidence was specifically cited by the court in holding that Chicago established its compelling interest in maintaining race-conscious remedies for discrimination in the construction market.

4. Anecdotal evidence of discrimination

IDOT considered and relied upon several sources of anecdotal evidence of discriminatory barriers to full and fair opportunities for DBEs to compete for its contracts. First, the testimony in the *Northern Contracting* trial provided ample un rebutted evidence of the discrimination still experienced by minority and women business owners in IDOT’s construction marketplace. Contractors testified that they experienced bias in bidding work as both prime contractors and subcontractors; that prime contractors who solicited them on projects with DBE goals rarely or never solicit them on contracts without goals; and that lenders and sureties sometimes discouraged them from growing their businesses and may have charged DBEs higher rates than their white male counterparts. DBEs further testified that the Program is essential to their continued business survival. Without DBE goals, they would receive little or no work on IDOT projects.

DBEs presented similar testimony to IDOT substantiating discrimination by IDOT’s prime contractors at the Department’s 2004 hearings on its Program. Particularly striking were the consistent and repeated statements from qualified DBEs that prime contractors who regularly use them on projects with DBE goals refuse to even solicit them for bids on projects without goals. After describing their business credentials, work history and awards, citations and honors, these witnesses identified by name over 20 of the most dominant IDOT construction and consultant prime contractors who regularly engage in this practice. DBEs were unanimous that without mandated good faith efforts to meet contracting goals, they would receive few, if any, public subcontracts. Some DBEs also discussed the barriers to transitioning to prime contract work, making the continuation of race-conscious subcontracting measures especially critical to their firms’ survival. The representative from the Illinois Roadbuilders Association also supported the need for the Program and the problem of insufficient bid solicitations. He acknowledged that the availability and capacity of DBEs is increasing, and stated that approximately 20% of the organization is now comprised of minority and women members.

In response to the testimony that DBEs suffer disparate treatment in receiving prompt payment by prime contractors, IDOT reviewed lien and bond claims for FFY 2003 and FFY 2004. DBEs filed 40.6% of the claims during that period but received only 22% of the subcontract awards and 22% of the subcontracting dollars. This large disparity suggests that prime contractors disproportionately fail to pay or to pay promptly socially and economically disadvantaged firms.

Further, as established by the un rebutted trial testimony in *BAGC*, minorities and women continue to face significant obstacles to entering into and succeeding in the construction industry. These include: the pervasive pattern of general contractors refusing to allow ready, willing and able minority- or women-owned firms to submit bids and compete for subcontracts on the same terms as majority-owned firms; the use by contractors of racial or gender epithets in refusing to deal with minority- and women-owned subcontractors; barriers to entry of minorities and women into the construction trades; disparate treatment of minority- and women-owned firms by unions; lack of mentoring opportunities and networking relationships to build skills and business contacts; overt harassment on the job site from White male employees and from majority-owned prime contractors; bid shopping; slow pay or no pay beyond that experienced by majority-owned firms; substitutions by prime contractors with non-DBEs post-award; higher performance standards not applied to majority-owned contractors; denial of bonding and financing or payment of higher rates than non-DBEs; and discrimination in price and delivery by suppliers.

In revising its M/WBE Program for construction contracts, the City Council of the City of Chicago conducted extensive hearings in the spring of 2004. In addition to the expert statistical evidence discussed above, numerous witnesses described discriminatory barriers to their success in the construction industry, and several groups submitted reports detailing the experiences of minorities and women with discrimination by prime contractors, banks, bonding companies, unions and other segments of the industry.

5. DBE utilization in race-neutral programs

One indicator of the need to continue to apply race-conscious measures is the participation of DBEs in the absence of those measures. The results of unremediated markets were an important component of the Department's defense of the DBE Program in the *Northern Contracting* trial. The precipitous decline in DBE participation after the Minnesota Department of Transportation's (MnDOT) DBE program was enjoined was noted by the courts in holding the revised Part 26 and MnDOT's implementation of the new regulations to be constitutional. Likewise, expert testimony in the *BAGC* trial documented the experiences of state and local governments whose race-conscious programs have either been enjoined or that do not set goals on locally-funded transportation contracts. In the absence of DBE programs, utilization of minority- and women-owned construction firms dropped dramatically below availability in all jurisdictions, including Cook County, Illinois. For the twelve months ending in December 2003, minorities and women received 4.78% of Cook County's construction contracts; prior to the injunction, the County had met its goals for 30% MBE and 10% WBE participation.

In addition, the experience of the Illinois State Toll Highway Authority is particularly instructive. The Authority's service area is encompassed by IDOT's District 1. Until very recently, it had a voluntary goal of awarding 15% of its prime and subcontracting dollars to DBEs. Operating in the same market for highway contracts as IDOT's District 1, the Tollway awarded 1.3% of its contracts to DBEs in 2002 (none as prime contractors), and 0.9% in 2003 (two as prime contractors). IDOT awarded 14.2% of its District 1 contracts to DBEs in 2002; 13.7% in 2003; and 17.8% through June 2004.

These data also mirror the results of IDOT's Zero Goals experiment. Like all the other agencies, utilization of DBEs on IDOT's contracts without goals was marginal.

The participation of DBEs on contracts with the Missouri Department of Transportation (MoDOT) is also probative, especially since many firms seek to work on both IDOT and MoDOT projects in the St. Louis area. Between July 2002 and July 2003, MoDOT achieved 7.68 % race-conscious and 1.36% race-neutral DBE utilization on its federally-assisted projects. For the same period on its state-funded contracts for which no goals may be set, DBE utilization was 1.68% as subcontractors and 1.68% as prime contractors.

6. Step 2 adjustment evaluations

The Department determined that the past participation of DBEs should not be used to adjust the Step 1 base figure. First, there is no evidence that DBEs are being overutilized relative to their availability and capacity. To the contrary, the Department reviewed extensive evidence, including that proffered at the *Northern Contracting* trial, that firms owned by minorities and women are available to do more, not less, work, and the Department's utilization of DBEs has increased in recent reporting periods. Therefore, relying upon past participation to define current capacity in determining the goal for a non-discriminatory market is inapposite for IDOT.

All of the evidence described above supports the qualitative judgment that, but for the continuing effects of discrimination, the availability of minorities and women to participate on IDOT's contracts would be considerably higher than 22.77% in a race-neutral market. The IDOT Study provides a quantitative estimate of the degree to which discriminatory factors artificially depress DBE participation in the marketplace. While the statistical disparities established by the IDOT Study could serve as the basis for an upward adjustment of the base figure, for an overall goal of 27.51%, the Department believes that the increase over prior years' goals to 22.77% is a plausible, lower bound estimate of DBE availability as defined by Judge Pallmeyer in the *Northern Contracting* case, and is currently sufficient to meet the objective of further remedying discrimination against DBEs.

II. Projection of Race-Neutral vs. Race-Conscious Goal Attainment

The Department will meet the maximum feasible portion of its overall goal through race-neutral means. Ongoing initiatives seek to reduce discriminatory barriers, increase capacity and level the playing field for the participation of DBEs and other small contractors. They are also designed to assist IDOT in meeting the increased goal for DBE participation as prime contractors and subcontractors and to arrest the decline in race-neutral participation on its contracts.

A. Race-neutral initiatives

1. Emerging contractors support initiatives

To increase competition for the Department's prime contracts and opportunities for DBEs and newer, smaller firms, IDOT is taking several steps to reduce barriers to participation as prime contractors. These include: reviewing the criteria for prequalification to reduce any unnecessary burdens; unbundling large contracts; and seeking FHWA approval of allocating some federal aid contracts for bidding only by firms meeting the Small Business Administration's definitions for small businesses.

2. Bonding and financing assistance

IDOT also adopted a bonding and financing assistance initiative for DBEs and other emerging contractors to meet prequalification and other requirements and to increase their current capacities to perform Department contracts and subcontracts. This program provides graduates with guaranteed bonding and lines of credit, thereby addressing two elements of the market where DBEs experience disparate treatment.

3. Mentor-protégé program

To increase DBE and small business capacities, IDOT has proposed for USDOT approval an effective Mentor-Protégé Program. This Program will provide DBEs and other small contractors the opportunity to work with established firms to enhance their capabilities to perform prime contracts.

4. Complaint procedures

The Department adopted a procedure to process complaints of discrimination in the operation of the Program and against contractors receiving IDOT contracts. This will ensure prompt, uniform and fair responses to allegations of unlawful conduct so that DBEs, non-DBEs and interested persons can have confidence in the integrity of IDOT's operations.

5. Non-discrimination assurances

To ensure that its prime contractors are providing full and fair opportunities for DBEs to compete and succeed, IDOT mandates as part of its prequalification process that applicants regularly maintain and make available at IDOT's request evidence that they are soliciting and evaluating subcontractors on a non-discriminatory basis in their daily business activities in the public and private sectors.

6. Prompt payment

The Department continues to enforce its prompt payment provisions and processes. It impresses upon its personnel and prime contractors the necessity and importance of meeting these requirements.

7. Outreach

The Department has implemented an extensive outreach program to attract additional DBE participation and to assist those businesses to become competitive in a race-neutral environment. It is further contacting firms identified as possible Program participants to encourage their applications and assist with meeting eligibility criteria.

8. Business development assistance

The Department retains a network of consultants to provide management, technical, technology and financial services to DBEs and other small businesses to increase their knowledge and competitiveness. Additionally, specialized targeted assistance is being provided to DBEs in District 4/I-74 and District 8/St. Clair and Madison Counties to increase their abilities to bid competitively and perform satisfactorily on construction projects.

9. Networking

The Department sponsors networking sessions throughout the state to encourage cooperation and participation on major construction projects. It is also cooperating with a statewide network of 20 Small Business Development Centers administered by the U.S. Small Business

Administration and the Illinois Department of Commerce and Economic Opportunity to provide information and training to DBEs and small businesses.

10. Information sharing

The Department continues to develop and expand its website as a valuable source for information and communication. The Contractor's Market Place provides an electronic bulletin board where prime contractors, subcontractors and suppliers can communicate about quotes on specific letting items and work categories. Information is organized by letting date and posted in an easy-to-read report format and updated daily.

11. Stakeholder inclusion

As part of IDOT's partnering with minority and women business associations and industry associations, the Small Business Advisory Committee (SBAC) works with the Department regarding the DBE program. Industry associations representing prime contractors and DBE interests, from both geographic and special interest perspectives, serve on the SBAC.

B. Estimate of Race-Neutral Participation

IDOT will meet the maximum feasible portion of its overall aspirational goal through these race-neutral measures. While the Department's current vigorous race-neutral efforts will continue and new initiatives are being implemented, contract goals are needed to ensure non-discrimination and to level the playing field for DBEs.

To estimate the portions of the goal to be met through race-neutral and race-conscious measures, the Department evaluated past race-neutral DBE participation as defined in §26.51(a). The median of IDOT's achievement of its goal through race-neutral means for FFY 2003, FFY 2004 and the first six months of FFY 2005 is 2.03%. Therefore, IDOT projects that it will meet 2.03% of its overall goal of 22.77% through race-neutral measures and 20.74% of its overall goal through race-conscious contract goals.

IDOT will monitor DBE participation throughout the year to adjust its use of contract goals to ensure that their use does not exceed the overall goal.

III. Public Participation

To satisfy the public consultation requirements of the regulations, the Department provided copies of its proposed submission to numerous stakeholders who may have information concerning the availability of DBEs and non-DBEs, the effects of discrimination on opportunities for DBEs, and IDOT's efforts to establish a level playing field for DBE participation, for their review and comments, as listed in Attachment B. We will evaluate any comments received and make changes to our proposed goal, if warranted. We are also publishing a notice of our goal and request for comments in our usual media outlets.

In addition, the Department continues its on-going dialogue with many individuals, minority organizations, women's groups and contractor associations that have a stake in the operation and success of the Program. The Department has recently created an Economic Opportunity Focus Group to advise it on current issues and suggest solutions to ensure equal opportunities for all communities and stakeholders.